

Office of Chief Counsel
Internal Revenue Service

memorandum

CC:WR:NCA:SAC:TL-N-5027-99
JLMcPherson

date: SEP 15 1999

to: Thelma Fisher
Taxpayer Advocate
Problem Resolution Unit
5880 Nolensville Rd., Stop 112
Nashville, TN 37211

from: JEREMY L. MCPHERSON
Attorney

subject: [REDACTED] and [REDACTED]
Allocation of Joint Estimated Tax Payments

This is in response to your request for advice regarding the appropriate allocation of estimated tax payments which [REDACTED] sent to the Internal Revenue Service for the tax year [REDACTED].

ISSUE:

When joint estimated tax payments are made by taxpayers residing in California (a community property state), and the taxpayers later file separate returns, and the spouses cannot agree about the proper allocation of the estimated tax payments, and it is not clear whether the payments were made with community property funds, how should the Service divide the estimated tax payments between the spouses?

CONCLUSION:

The first three (joint) estimated tax payments (\$[REDACTED] in total) should be allocated between [REDACTED] and [REDACTED] in the same ratio as the separate [REDACTED] tax liability of each spouse bears to the sum of their separate tax liabilities. See Treas. Reg. § 1.6015(b)-1(b).

FACTS:

Joint estimated tax payment for the [REDACTED] tax year were received by the Internal Revenue Service in the following amounts and on the following dates:

DateAmount

[REDACTED]

\$ [REDACTED]

All three payments were originally posted to [REDACTED]'s social security number.

[REDACTED] and [REDACTED] each filed a [REDACTED] tax return as a married person filing separately. [REDACTED] allegedly attached a statement to his return, stating that the three estimated tax payments listed above were to be divided equally between him and [REDACTED]. The Service transferred half (\$ [REDACTED]) of each of the above-listed estimated tax payments from [REDACTED]'s [REDACTED] account to [REDACTED]'s [REDACTED] account.¹

[REDACTED] filed his [REDACTED] tax return on or about [REDACTED], and reported a [REDACTED] tax liability of \$ [REDACTED]. On [REDACTED], the Service issued a manual refund to [REDACTED] in the amount of \$ [REDACTED] (estimated tax payments of \$ [REDACTED] less tax liability of \$ [REDACTED]).

[REDACTED] requested an extension of time to file her [REDACTED] tax return; she made a payment of \$ [REDACTED] with her request for an extension, on or about [REDACTED]. The Service received the [REDACTED] tax return of [REDACTED] on [REDACTED]. [REDACTED] reported tax of \$ [REDACTED] on her return. The following payments had been applied to her [REDACTED] account as of the date her [REDACTED] tax was assessed:

DateAmountType of payment

[REDACTED]

\$ [REDACTED]
[REDACTED]
\$ [REDACTED]

ES, transferred-in
ES, transferred-in
ES, transferred-in
ES, transferred-in
with extension request

[REDACTED]'s [REDACTED] account was overpaid by \$ [REDACTED] as of [REDACTED], the date her [REDACTED] tax was assessed. The

¹ At the same time, the Service transferred a fourth estimated tax payment, \$ [REDACTED] made on [REDACTED], from [REDACTED]'s [REDACTED] account to [REDACTED]'s [REDACTED] account. [REDACTED] and [REDACTED] apparently agree that this payment belonged to [REDACTED].

Service applied \$ [REDACTED] to her [REDACTED] estimated tax, and refunded \$ [REDACTED] to her on [REDACTED].

In [REDACTED], [REDACTED] provided a "STATEMENT UNDER PENALTY OF PERJURY" to the Internal Revenue Service. She stated that she (separately) had made all of the [REDACTED] estimated tax payments (three in the amount of \$ [REDACTED] each, and a fourth in the amount of \$ [REDACTED]). She said that the payments were made using estimated tax vouchers in her name alone. She enclosed with the statement copies of her cancelled checks, and copies of estimated tax vouchers in her name alone.

Based (apparently) on the allegations of [REDACTED] in her sworn statement, on [REDACTED] the Service transferred from [REDACTED]'s [REDACTED] account to [REDACTED]'s [REDACTED] account all of the [REDACTED] estimated tax payments which had not already been moved from his account to hers, as follows:

Date

Amount

[REDACTED]

\$ [REDACTED]

This put [REDACTED]'s [REDACTED] account into a debit balance, due to the fact that these estimated payments (less the amount of his [REDACTED] tax) had already been refunded to [REDACTED].

The Service transferred these same estimated tax payments back into [REDACTED]'s [REDACTED] account in [REDACTED] and transferred these same estimated tax payments back off his [REDACTED] account in [REDACTED].

The Service issued a refund to [REDACTED] in the amount of \$ [REDACTED] (\$ [REDACTED] plus interest of \$ [REDACTED] on [REDACTED] [REDACTED]).

In [REDACTED], the Service obtained the actual estimated tax vouchers which accompanied the four [REDACTED] estimated tax payments, and determined (contrary to the statement of [REDACTED]) that all of the vouchers were in the names and social security numbers of both [REDACTED] and [REDACTED].

[REDACTED] provided evidence that the estimated tax payments came from a bank account in her name, which the divorce court had awarded to her (after the disputed payments had been made). [REDACTED] provided evidence that he had made payments to [REDACTED], and he claims that those payments were intended by the two of them to be applied to their joint [REDACTED].

estimated tax. [REDACTED] argues that the funds were community property; [REDACTED] insists that payments were all made with her separate funds.

ANALYSIS:

An estimated tax payment made in the name of only one spouse must be credited to the account of that spouse if that spouse files a separate income tax return. Janus v. United States, 557 F.2d 1268 (9th Cir. 1977). If joint estimated tax payments are made but separate income tax returns are filed, the Internal Revenue Service may divide the estimated tax payments between the spouses. Morris v. Commissioner, T.C. Memo. 1966-245 (a case involving community property, but estimated tax paid in the husband's name alone).

Treas. Reg. § 1.6015(b)-1(b) contains rules for allocating joint payments of estimated tax where a joint "declaration" of estimated tax was filed, but the spouses later filed separate income tax returns. The regulation states (in pertinent part) as follows:

In the event the husband and wife fail to agree to a division, such payments shall be allocated between them in accordance with the following rule. The portion of such payments to be allocated to a spouse shall be that portion of the aggregate of all such payments as the amount of tax imposed by chapter 1 (other than section 56) shown on the separate return of the taxpayer ... bears to the sum of the taxes imposed by chapter 1 (other than section 56) shown on the separate returns of the taxpayer and his spouse

In other words, the regulation provides that, when the spouses cannot agree on the division of payments, the Service will determine the husband's share according to the following formula:

$$\begin{array}{rcl} & \text{H's income tax liability} & \\ + & \text{W's income tax liability} & \\ = & \text{Combined tax} & \end{array}$$
$$\begin{array}{l} \text{H's tax divided by Combined tax} \\ \text{equals H's percentage of estimated payments.} \end{array}$$

A similar computation would be used to determine the wife's share.

Regulation 1.6015(b)-1(b) makes no distinction between estimated tax payments made from community funds and payments made from separate funds.

Section 3(15)(129)5.34 of the Internal Revenue Manual (dealing with allocation of estimated tax payments) states that "[i]n community property states, state law determines if income is separate or community property. Property designated by the state as community property must be allocated equally (50%) between the TPs." Unfortunately, this manual provision is helpful only where state law has unquestionably "designated" a particular payment as community property. The Service is rarely in a position to know if this is true. In this case, the parties disagree about the source of the funds, and the evidence provided to the Service is conflicting.

Where (1) joint estimated tax payments have been made, (2) followed by the filing of separate returns by the spouses, (3) and where the spouses do not agree on an allocation of the estimated tax payment, and (4) the Service cannot tell whether estimated tax payments are, or are not, community property, the Service should allocate the payments according to Treas. Reg. § 1.6015(b)-(b).

In this case, [REDACTED]'s [REDACTED] tax was \$ [REDACTED] and [REDACTED]'s [REDACTED] tax was \$ [REDACTED]. The sum of their tax liabilities was \$ [REDACTED]. [REDACTED]'s tax was [REDACTED] percent of their combined liabilities (\$ [REDACTED] divided by \$ [REDACTED]). His allocated share of the \$ [REDACTED] of disputed estimated tax payments would thus be \$ [REDACTED] (\$ [REDACTED] times [REDACTED] percent).

The Service should transfer \$ [REDACTED] back to [REDACTED]'s [REDACTED] account from [REDACTED]'s [REDACTED] account. This will leave [REDACTED]'s account in a debit balance. This will also cause [REDACTED]'s [REDACTED] account to go into a debit balance.

THE TAXPAYERS' RECOURSE

This type of dispute between estranged or ex-spouses often creates a "no-win" situation for the Service. In all likelihood, no one will be happy with the result. But the issue boils down to a property dispute between [REDACTED] and [REDACTED]. They divided their other marital property by resort to state courts; they may wish to have those same courts decide how the [REDACTED] estimated tax payments should have been divided. But the Service should not make further transfers between the accounts, after those suggested above. To the extent that a state court decides that [REDACTED] was entitled to more than \$ [REDACTED] of the payments, he would have a cause of action against [REDACTED]. But he will be responsible for paying the amount due on his [REDACTED] account (as will [REDACTED] as to her account).

ASSESSMENT AND COLLECTION ISSUES

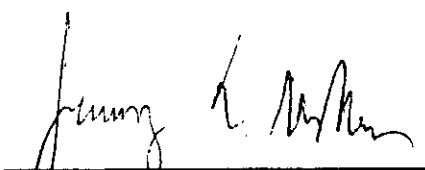
The Service has issued erroneous refunds to both [REDACTED] and [REDACTED] for the [REDACTED] tax year, as a result of the transfers of the estimated tax payments between accounts. Allocating the estimated tax payments as suggested above will result in [REDACTED]'s [REDACTED] account being underpaid by \$ [REDACTED] (not counting interest and penalty amounts); and in [REDACTED]'s [REDACTED] account being underpaid by \$ [REDACTED] (also not counting interest or penalty).

The erroneous refunds are "non-rebate." See General Counsel Memorandum (GCM) 36263 (copy enclosed), as modified by GCM 36624 (copy enclosed). An issue exists whether the balances on the [REDACTED] accounts of [REDACTED] and [REDACTED] may be collected using normal IRS collection techniques.

I.R.C. § 6201(a)(3) provides as follows:

ERRONEOUS INCOME TAX PREPAYMENT CREDITS.- If on any return or claim for refund of income taxes under subtitle A there is an overstatement of the credit for income tax withheld at the source, or of the amount paid as estimated income tax, the amount so overstated which is allowed against the tax shown on the return or which is allowed as a credit or refund may be assessed by the Secretary in the same manner as in the case of a mathematical or clerical error appearing upon the return, except that the provisions of section 6213(b)(2) (relating to abatement of mathematical or clerical error assessments) shall not apply with regard to any assessment under this paragraph.

The Service may wish to assess \$ [REDACTED] against [REDACTED]'s [REDACTED] account under the provisions of I.R.C. § 6201(a)(3), and assess \$ [REDACTED] against [REDACTED]'s [REDACTED] account under the same section. If these assessments are made, the Service may then proceed to collect the unpaid amounts (or take other action, as appropriate) following normal procedures. We suggest that you consult with your local District Counsel regarding assessment and collection matters in this case.


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Enclosures:

GCM 36263 and GCM 36624.